


A Discussion on Utah's Housing

An expert shares
his view on the
current state of
Utah's construction
environment.



Jim Wood is the director of the Bureau of Economic and Business Research at the University of Utah. One of the Bureau's tasks is monitoring Utah's construction market, with a focus on assembling and quantifying permits and valuation for new housing construction, along with nonresidential construction. This task brings Jim in contact with many of Utah's builders. Jim recently took the time to talk with me about the current state of Utah's construction environment:

MK: *What is your summary of the current state of the Utah housing market?*

JW: On the residential side, sales of new homes have nearly ground to a halt. This is quite a contrast with the pace of new home sales and construction of the past several years. Obviously, builders are concerned because they are the ones with the greatest exposure. They have houses to move. Traffic, qualifications, and sales are all down. Their inventory is growing. They're experiencing homes sold and

then suddenly not sold, as buyers either pull out or lose their financing. Naturally, builders are reluctant to continue to aggressively build. They're willing to finish the houses they have ongoing, which can carry them into the spring, but after that, they seem to be hunkering down.

New home, single-family permitting is down significantly, possibly by as much as 30 percent for this year. However, multi-family permitting is strong, as is the condominium market. But I do have some concerns about the condo market and its potential to overbuild going forward.

MK: *Why is this residential slowdown happening?*

JW: Various factors can influence a market, but this does not appear to be a problem of building too many houses in relation to too few households. Homebuilding seems to be in line with the formation of new households in Utah—they seem to be in balance. Instead, this is a credit market situation. The sub-prime meltdown is all over

the news and a pessimistic psychology has now entered the market. Lenders are making it harder to qualify for loans, so even willing buyers are being turned down. But the psychology itself tends to have a powerful influence on the market, even if that psychology might be distorted. People hear the bad national news and translate it into Utah news. People start to think Utah home prices will now come down, and therefore they settle into a wait mode, expecting cheaper deals in the future. But in my 30-plus years of watching this market, home price depreciation in Utah is very, very rare. That's not to say it can't happen, but expecting it to happen seems to be betting against the odds. Even if there is a current dam blocking home sales and movement, there is a continuing flow of developing households in Utah who need a home. Prices do appear to no longer be rising, but Utah's demographic pressures and robust economy suggest that price declines as experienced nationally are not a foregone conclusion here.

The grey area in this picture is that we don't have a history for this type of mortgage pullback, therefore we don't have an example to gauge against. Unless the global financial markets freeze up, I would anticipate that the lending markets should come back to life next year. Utah's demographics suggest that the demand for housing will remain strong. We still have several more years of anticipated strong household formation as the influential demographic surge of 20-to-30-year-olds into Utah's labor market continues to unfold. Utah's strong economy and strong job growth certainly help to augment and stabilize these household formations.

MK: *Do you feel there was much speculative building as is the bane of some of our western neighbors?*

JW: Some builders feel that there was, but I don't think I see that in the numbers. Of course our process doesn't identify speculative building,

but you have to try and put houses and household numbers together. Let's look back at the recent permitting buildup, which ran from 2003 and peaked in 2005. I see two factors influencing that building spike. First, we had no house-price appreciation from 1998 to 2003, therefore houses hadn't become overpriced. Second, we had a huge influx of first-time homebuyers in this decade as Utah's 1980 baby boom came of home-buying age. The economy shut them out of the market at this decade's inception, but with the economy improving, beginning in 2003, they jumped into the housing market in a big way.

The permitting peak was in 2005, so let's look at that year's numbers. The Governor's Office of Planning and Budget estimates that there were 24,000 new Utah households formed in that year. The number of permits issued for dwelling units was just over 28,000. Factor in pent-up demand from previous years and the overall house-building/household-formation picture does not seem out of line. A previous big speculative-building year was back in 1977, when 23,300 permits were issued. Utah's population then was only 1.3 million people. In 2005, the permits issued were just over 28,000, slightly higher than in 1977, but the Utah population has now grown to 2.7 million. Homebuilding in relation to the population doesn't seem out of line.

MK: *What about Utah home prices? Are they overvalued?*

JW: The housing price index from the Office of Federal Housing Enterprise Oversight would suggest not. Utah's current housing price index is right around the national average, which is a position we have been at many times before and our income levels seem comfortable with. Housing prices rose rapidly in the last two years, with the Wasatch Front recently leading the nation in housing price appreciation. That gets much exposure, but if we

put it into a five-year perspective, the housing price increase becomes more subdued. In relation to other western states, only Colorado's housing price appreciation has been lower than Utah's over that time. All we have done over the past five years is have our housing prices catch up with the national average. The high-profile part is that we did it within a two-year window. The current feel I'm getting is that Utah housing price appreciation is rapidly slowing, so it looks like prices have peaked.

MK: *Can the nonresidential market make up for the housing slowdown?*

JW: Nonresidential activity in Utah is certainly booming, and it probably won't see its permitting peak until late 2008 or even 2009. There is nonresidential activity all over Utah, and its boom certainly helps to cushion any drop-offs that may occur in the residential market. But it's not certain that all residential construction workers can automatically go work in nonresidential. I'm not sure that their skills transfer that easily. It's interesting though, that even with the national housing market slowing so much, national construction employment numbers are holding steady. Nonresidential construction is doing well nationally, so I guess that serves as an example of how nonresidential can pick up the slack. 📍

